80-2143

No. _____

Office-Supreme Court, U.S.
FILED
JUN 17 1981
ALEXANDER L. STEVAS,
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

TRANSCONTINENTAL GAS PIPE LINE CORPORATION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIAN E. O'NEILL, *Senior Vice President and General Counsel*
R.V. LOFTIN, JR.
TRANSCONTINENTAL GAS PIPE LINE CORPORATION
P.O. Box 1396
Houston, Texas 77001

THOMAS F. RYAN, JR.*
RICHARD T. BOONE
ANDREWS, KURTH, CAMPBELL & JONES
1747 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
(202) 861-7400

Attorneys for
Transcontinental Gas Pipe Line Corporation

June 17, 1981

*Counsel of Record.

PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D.C.

QUESTIONS PRESENTED

1. Whether, if the Commission is required to satisfy Section 5(a) of the Natural Gas Act prior to changing a settled component of a pipeline's rates (such as the method of allocating costs among zones), the Commission is also required to satisfy Section 5(a) prior to reducing a pipeline's previously allowed level of rate of return on common equity.

2. Whether the Commission may substantially reduce previously allowed levels of rate of return on equity without explanation of such departure from precedent and with no claim of changed circumstances justifying such departure.*

---

* In addition to the parties named in the caption of this case the following were parties to the proceeding in the court of appeals: Atlanta Gas Light Company, Brooklyn Union Gas Company, Carolina Pipeline Company, Columbia Gas Transmission Corporation, Commonwealth Gas Pipeline Corporation, Consolidated Edison Company of New York, Inc., Elizabethtown Gas Company, Long Island Lighting Company, National Fuel Gas Supply Corporation, North Carolina Natural Gas Corporation, North Carolina Utilities Commission, Philadelphia Electric Company, Philadelphia Gas Works, Piedmont Natural Gas Company, Inc., Public Service Commission of the State of New York, Public Service Company of North Carolina, Inc., Public Service Electric and Gas Company, South Jersey Gas Company and Washington Gas Light Company.

TABLE OF CONTENTS

	PAGE
OPINIONS BELOW	2
JURISDICTION	3
STATUTORY PROVISIONS INVOLVED	3
STATEMENT OF THE CASE	3
REASONS FOR GRANTING THE WRIT	8
1. The Court Should Review The Entire Case To Resolve The Inconsistent And Conflicting Standards Applied By The Court Below	8
2. The Resolution Of The Questions Presented Is Necessary To Provide Guidance To Courts Of Appeals On The Proper Standard Of Review Of Administrative Decisionmaking	13
CONCLUSION	17
APPENDIX A	1a
APPENDIX B	3a
APPENDIX C	4a

TABLE OF AUTHORITIES

CASES: PAGE

Atlantic Refining Co. v. *Public Service Commission*, 360 U.S. 378 (1959) 12

Colorado Interstate Gas Co. v. *Federal Power Commission*, 324 U.S. 581 (1945) 14

Columbia Gas Transmission Corp., et al. v. *Federal Energy Regulatory Commission*, 628 F.2d 578 (D.C. Cir. 1979) 7, 11, 16

Federal Power Commission v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) 14

Minnesota Power & Light Co. (Opinion No. 87), Docket No. ER77-427 (June 24, 1980) 16

Panhandle Eastern Pipe Line Co. v. *Federal Power Commission*, 236 F.2d 606 (3d Cir. 1956) 16

Permian Basin Area Rate Cases, 390 U.S. 747 (1968) ... 14

Securities and Exchange Commission v. *Chenery Corp., et al.*, 318 U.S. 80 (1943) 15

United Gas Pipe Line Co. v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) 10, 15

STATUTES AND REGULATIONS:

Natural Gas Act, 15 U.S.C. 717 *et seq.* .....*passim*
Section 4
Section 5(a)

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

No. _____

TRANSCONTINENTAL GAS PIPE LINE CORPORATION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

On May 18, 1981 in the captioned proceedings the Solicitor General, on behalf of the Federal Energy Regulatory Commission (Commission), the North Carolina Utilities Commission (NCUC) and North Carolina Natural Gas Corporation, *et al.* (NCNG, *et al.*) petitioned for writs of certiorari to review a portion of the judgment of the United States Court of Appeals for the District of Columbia Circuit in *The Public Service Commission of the State of New York, et al.* v. *Federal Energy Regulatory Commission,* 642 F.2d 1335 (D.C. Cir. 1980). Transcontinental Gas Pipe Line Corporation (Transco) hereby cross-petitions for a writ of certiorari

to review a separate but inconsistently decided portion of the same judgment so that, if the foregoing Petitions are granted, the Court will have the entire case before it in order that it may apply the same principles to the two issues.[1]

OPINIONS AND ORDERS BELOW

The opinion of the court of appeals (FERC Pet. App. A, at pp. la-27a[2]) is reported at 642 F.2d 1335. The orders of the Commission which are pertinent to the instant Cross-Petition are not reported and appear in Appendices A and B hereto, at pp. la-2a and p. 3a, respectively. The decision of the administrative law judge which was adopted by the Commission is not reported and appears in Appendix C hereto, at pp. 4a-19a.

---

[1] In accordance with Rule 28.1, Transco states that it is a wholly owned subsidiary of Transco Companies, Inc. and has the following subsidiaries or affiliates: Alapost; Border Gas, Inc.; C&T Pipeline, Inc.; Dixie Pipeline Company; Gasco Insurance Company, Limited; TCI Realty, Inc.; Towtrans Company; Transco Coal Gas Company; Transco Energy Company; Transco Exploration Company; Transco Gas Supply Company; Transco Hydrocarbon Company; Transco International N.V.; Transco LPG Company; Transco Offshore Pipeline Company; Transco Propane Supply Company; Transco Production of Canada, Ltd.; Transco Propane Products Company; Transco Terminal Company; Trans-Jeff Chemical; Tubexpress Systems, Inc.

[2] Copies of the opinion and orders of the court below and the pertinent statutory provisions required by Rule 21.1(k) appear in an Appendix to the Petition for a Writ of Certiorari filed on May 17, 1981 by the Solicitor General on behalf of the Commission in 80-1937. In this Cross-Petition, references to "the Commission" or citations to "FERC Pet." are to that pleading. The portions of the opinion of the court below which are pertinent to the issues raised in this Cross-Petition are reported at 642 F.2d at 1348-1351, and appear at FERC Pet. App.A, pp.21a-26a and FERC Pet.App.C, pp.32a-33a.

JURISDICTION

The judgment of the United States Court of Appeals for the District of Columbia Circuit was entered on September 24, 1980. A timely petition for rehearing and a suggestion for rehearing *en banc* by Transco were denied on December 18, 1980. NCUC, on May 15, 1981, and the Commission and NCNG, *et al.*, on May 18, 1981, petitioned this Court for writs of certiorari in this case. Transco received NCUC's Petition on May 18, 1981 and received the Petitions of NCNG, *et al.*, and of the Commission on May 21, 1981. The instant Cross-Petition to those Petitions is filed pursuant to Rule 19.5 of this Court's Rules. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

Sections 4 and 5(a) of the Natural Gas Act, 15 U.S.C. §§717c and 717d(a), are set forth in FERC Pet. App. I, at pp. 63a-65a.

STATEMENT OF THE CASE

Transco is a major interstate natural gas pipeline system which is subject to regulation as to service and rates by the Commission under the Natural Gas Act. Transco owns and operates extensive pipeline facilities which are utilized to transport gas from the sources of Transco's gas supplies, located in the Gulf Coast area, primarily to wholesale markets along the eastern seaboard of the United States from Atlanta, Georgia to New York City.

The questions presented by this Cross-Petition and the Petitions filed by the Commission and other parties arise from a proceeding in which Transco initiated a

general rate increase pursuant to Section 4(d) of the Natural Gas Act on July 30, 1976. After suspension by the Commission pursuant to Section 4(e) of the Act, Transco's increased rates became effective, subject to refund, on February 1, 1977.[3] As part of its rate increase, Transco proposed an increase in its allowed rate of return on equity capital from the previously allowed level of 14.75 percent to 17.00 percent. Transco did not propose any changes in the long-standing method used to allocate costs among the rate zones on its system. The increase in Transco's proposed equity return was occasioned by increased risks associated with Transco's business resulting from the severe shortage of natural gas as well as overall economic conditions characterized by rapidly increasing costs and rampant inflation. Ultimately, most of the issues in the proceeding before the Commission were resolved by settlement, but the issue of the justness and reasonableness of Transco's proposed increase in its allowed rate of return and a complaint that Transco's existing zone rate differentials were unlawful were reserved for separate hearings and decision.

In a separate rate of return hearing, Transco introduced evidence in support of its claimed equity return of 17.00 percent. The staff of the Commission was the only other party to introduce evidence on the issue and recommended an equity return for Transco of 14.00 percent, or three-quarters of a percentage point *below* the level of equity return allowed by the Commission in Transco's three immediately preceding rate cases. On

---

[3] On July 1, 1977, Transco filed a superseding rate increase which, after suspension by the Commission, was allowed to become effective, subject to refund, on January 1, 1978. Therefore, the instant rates were effective for the eleven-month period from February 1, 1977 through December 31, 1977.

February 13, 1978, the administrative law judge (ALJ) issued an initial decision, holding that Transco's proposed rate of return of 17.00 percent was not justified and, notwithstanding his holding that "Transco poses greater risks to investors than does virtually any other pipeline company" (App. C, p. 14a), not only disallowed the entire proposed increase in return but also significantly reduced the previously allowed level of 14.75 percent to 14.00 percent.[4] In deciding the issue, the ALJ dismissed Transco's argument that there was no evidence of changed circumstances that would rationally permit any reduction from the 14.75 percent level of return on equity previously allowed to Transco with the statement that such previous allowances were produced by settlement and would not be considered. (App. C, p. 12a).

Transco appealed the ALJ's decision to the Commission, arguing that the ALJ had erroneously failed to consider Transco's consistently allowed rate of return on equity of 14.75 percent as the point of reference in evaluating the evidence of the Commission staff's witness, who gave no rationale whatsoever in support of his recommended reduction in previously allowed returns to Transco. Transco also argued that the ALJ had erred in several respects in evaluating Transco's evidence supporting the proposed increase in allowed equity return. Indeed, the ALJ's analysis in the initial decision was so cryptic that Transco contended the Commission could not determine from the initial decision the facts which were relied on by the ALJ or the reasoning, if any, based on such facts. Nevertheless, on August 30, 1979,

---

[4] The difference of 0.75 percentage points amounts to about $4.8 million in revenues for the eleven-month period the rates at issue were in effect.

the Commission, in a one-page order which contained no explanation for its decision, affirmed and adopted the decision of the ALJ. (App. A).

Transco appealed the Commission's rate of return orders to the court below. The Commission's decision on the zone rate differential issue was also appealed by representatives located in Zone 3[3] and, because of the coincidental timing of the separate decisions by the Commission, the two issues were consolidated in the court below. On September 24, 1980, the court below reversed the Commission's decision which rejected Transco's historical zone rate differentials, finding that the Commission had failed to satisfy the strictures of Section 5(a) of the Natural Gas Act before imposing its own cost allocation methodology. Specifically, the court held:

> Had Transco proposed any changes in them [the existing zone rate differentials], the Commission, acting under Section 4(e), could have approved the changes in whole or in part. *Section 4(e), however, cannot be used by the Commission to institute any change in a rate-making component, such as cost allocation, that does not represent at least partial approval of the change for which the enterprise had petitioned in its filing.* If the Commission seeks to make such changes, it has no alternative save compliance with the strictures of Section 5(a).

FERC Pet. App. C, pp. 32a-33a (emphasis supplied). However, with respect to the rate of return issue, the

---

[3] As more fully explained in the Petitions filed by the Commission, NCUC and NCNG, *et al.*, Transco's system is divided into three rate zones. The decision of the Commission in its Opinion No. 59 (FERC Pet. App. F, pp. 36a-52a), vacated by the court below, shifted significantly greater costs to Zone 3 from Zones 1 and 2 than the previous historical method of allocation.

court below, while paying lip-service to the Section 4-Section 5 dichotomy in analyzing the issue, erroneously held that the Commission had satisfied Section 5(a)'s requirements. Concerning the applicable legal standard on the rate of return issue, the court stated:

> [W]hen the Commission not only voids a proposed rate increase, but institutes a rate of its own under Section 5(a) rather than continuing the old rate in effect, it must advance substantial evidence to prove (1) that the old rate is unjust and unreasonable and (2) the Commission's proposed rate is just and reasonable.

FERC Pet. App. A, pp. 24a-25a n. 27. However, in sharp contrast to its detailed examination of the rationale offered by the Commission in Opinion No. 59 for rejecting Transco's historical zone differentials, the court below affirmed the Commission's cursory rate of return orders even though the Commission had *explicitly refused* to explain why Transco's previously allowed rate of return on equity had become unjust and unreasonable. Moreover, although the court below appeared to have recognized the applicability of Section 5(a) when the Commission proposes to reduce previously allowed rates of return, the court inexplicably held that its decision in *Columbia Gas Transmission Corp., et al* v. *Federal Energy Regulatory Commission,* 628 F.2d 578 (D.C. Cir. 1979), was inapplicable to rate of return determinations even though the *Columbia Gas* precedent was found to be fully applicable to other previously established rate components that the Commission proposes to change.

REASONS FOR GRANTING THE WRIT

1. The Court Should Review The Entire Case To Resolve The Inconsistent And Conflicting Standards Applied By The Court Below

Uniform decisionmaking requires that this Court grant the instant Cross-Petition if the Petitions submitted by the Commission and/or the other parties concerning the decision by the court below on zone rate differentials are granted. The Commission as well as the other petitioners have raised issues which not only bear on the discrete issue of cost allocation but also all other rate components, including rate of return. Since the court below appears to have analyzed both aspects of this case in the same fashion and yet resolved each in an inconsistent and conflicting manner, we believe that this Court should review the entire case if the Court determines to grant the petitions filed by the Commission or the other parties in order to prevent confusion in the administration of the Natural Gas Act.

While the court below has in Transco's view correctly decided with respect to the zone differential issue that as a matter of law the Commission must proceed under Section 5(a) of the Natural Gas Act to the extent that it proposes to institute a change in any rate component for which the regulated pipeline has not applied, the court has *not* been consistent in requiring the same observation of Section 5(a)'s requirements from the Commission with respect to the changes which it proposed in Transco's previously allowed rate of return on equity.[6]

---

[6] While Transco did propose an increase in its allowed rate of return and did not propose a change in its historical zone rate differentials, this factual difference is irrelevant to the procedures that the Commission is required to follow when proposing to reduce

In effect, the decision below erroneously holds that Section 5(a) establishes a legal standard which changes in meaning depending upon the subject matter to which its procedures are applied. It is therefore necessary that this Court issue the writ, if at all, to review the decision below on both the rate of return issue and the zone rate differentials issue to clarify the confusing and fundamentally inconsistent meaning which the court below has ascribed to Section 5(a) of the Natural Gas Act.

Section 5(a) of the Act allows the Commission to investigate the lawfulness of existing rate components and, only after finding that the rate or rate component so investigated is "unjust, unreasonable, unduly discriminatory or preferential," allows the Commission to determine the just and reasonable rate to be thereafter effective. This Court has previously addressed the fundamental powers of the Commission under Section 5(a) of the Act and differentiated such powers from those set forth in Section 4(e) of the Act:

> The powers of the Commission are defined by §§4(e) and 5(a). The basic power of the Commission is that given it by §5(a) to set aside and modify any rate or contract which it determines, after hearing, to be 'unjust, unreasonable, unduly discriminatory, or preferential.' *** It is simply the power to review rates and contracts made in the first instance by

---

Transco's *previously established* level of rate of return. The court below correctly distinguished between setting aside Transco's entire proposed increase and in reducing the previously allowed level of return. (FERC Pet. App. A, pp. 24a-25a n. 27). The Court's distinction is valid because pipelines should properly be allowed to propose increased rates of return without jeopardizing their pre-existing levels of return to any greater extent than such established levels are subject to investigation and prospective change under Section 5(a) of the Natural Gas Act.

> natural gas companies and, if they are determined to be unlawful, to remedy them. Section 5(a) would of its own force apply to *all* the rates of a natural gas company, whether long-established or newly changed, but in the latter case the power is further implemented by §4(e). All that §4(e) does, however, is to add to this basic power, in the case of a newly changed rate or contract . . ., the further powers (1) to preserve the status quo pending review of the new rate by suspending its operation for a limited period, and (2) thereafter to make its order retroactive, by means of the refund procedure, to the date the change became effective.

United Gas Pipe Line Co. v. *Mobile Gas Service Corp.*, 350 U.S. 332, 341 (1956). Thus, when the Commission proceeds under Section 5(a) rather than under Section 4, as the court below correctly held the Commission must when contemplating a reduction in the previously approved level of a pipeline's rate of return component, it must focus on the established rate component being investigated and make findings based on substantial evidence that such existing level is unjust or unreasonable. However, even a cursory reading of the Commission's rate of return order (App. C, p. 12a) evidences a total disregard by the Commission for the requirement to focus on the established rate of return allowed Transco in previous cases. In the face of the Commission's stated refusal to give a reasoned explanation for rejecting Transco's previous rate of return allowance, the affirmance of the Commission's rate of return orders is inexplicable.

Section 5(a) of the Natural Gas Act cannot have a different meaning with respect to rate of return determinations than it has with respect to cost allocation determinations by the Commission. Regardless of the subject matter, the structure of the Act fairly con-

templates that, once established, a pipeline's existing rates, and any component thereof, constitute the point of departure against which any contemplated or proposed change, whether it be an increase or a decrease, must be measured. *See, Columbia Gas Transmission Corp., et al.* v. *Federal Energy Regulatory Commission,* 628 F.2d 578, 585-586 (D.C. Cir. 1979). The court below held, however, that the principle of *Columbia Gas* did not apply to the Commission's proposed reduction of Transco's previously approved rate of return of 14.75 percent.[7] The court's attempted distinction of the requirements of *Columbia Gas* was based on the supposed fact that with respect to the zone rate differentials issue "the Commission was choosing between present practice and a discrete alternative" (FERC Pet. App. A, p. 25a), but that with respect to the rate of return issue the Commission was faced with an "infinitude of choices." (*Id.*). This attempted distinction is a makeweight. With respect to the zone rate differential issue, the administrative record below contained evidence supporting more than the two alternatives noted by the court. The number of alternatives confronting the Commission on a particular issue is simply irrelevant to the obligation to explain a rejection of the previously established rate component that the Commission proposes to change.

---

[7] The court below held that "[t]he Commission's conclusion that only rates between 13.5% and 14.3% are just and reasonable" (FERC Pet. App. A, p. 25a, n.27) fulfilled the requirement of Section 5(a) for findings that Transco's 14.75 percent return was unlawful. However, the referenced findings by the Commission were totally independent of any consideration of Transco's previously allowed return, the latter having been explicitly *not considered* by the Commission (App. C, p. 12a). In any event, such "finding" does not explain what, if anything, rendered the previously allowed level of return unlawful.

The determinative fact is that one, and only one, cost allocation method had been employed historically by Transco against which all other proposed methodologies could be judged. Similarly, a single, discrete rate of return allowance (*i.e.*, 14.75 percent) had been approved consistently in determining Transco's rates in previous cases and, under the *Columbia Gas* rule, this component represents the proper point of departure in analyzing both the need for and propriety of any change therein. That the Commission had consistently allowed a rate of return on equity of 14.75 percent in Transco's three immediately preceding rate cases establishes a no less concrete point of departure than the Commission's approval of Transco's historical zone allocation method in those cases. Given the similarity of the issues, therefore, there is no rational basis for the court below to have attempted *sua sponte* to characterize the Commission's prior approval of Transco's rate of return as somehow less than a settled, existing and lawful point of departure for reviewing any substantial reduction thereof.

The Petitions submitted by the Commission, NCUC and NCNG, *et al.*, each focus on the remedial consequences that may flow from the decision by the court below that the Commission must proceed under Section 5(a) of the Natural Gas Act rather than under Section 4 in situations where established rate components are proposed to be changed *sua sponte* by the Commission.[8] The characteristics of the remedy available under Section 5(a) of the Act have been previously recognized by this Court. *Atlantic Refining Co.* v. *Public Service Commission*, 360 U.S. 378, 389-390 (1959). A perceived inade-

---

[8] In Opinion No. 59, the Commission made its decision to change Transco's zone differentials effective on a prospective basis as if it were deciding the case under Section 5(a).

quacy of the remedial powers delegated by Congress to the Commission, however, cannot thwart the procedures that Congress has mandated the Commission to follow in reviewing the rates of natural gas companies; the character of the rate investigated, rather than the adequacy of the Commission's remedy, must determine the statutory provision under which the Commission must proceed. In any case, the statutory construction issue raised by the Commission and other petitioners is almost beside the point, because on the zone rate differential issue the alternative decisional ground of the court below, *i.e.*, that "[i]n any event, the evidence of record supporting [the Commission's prescribed method of cost allocation] falls short of substantiality" (FERC Pet. App. A, p. 21a), is clearly correct. This case presents, first and foremost, the threshold question whether the findings of the Commission on both rate issues, and the rationale and evidence supporting them, are consistent with and adequate under the Natural Gas Act and general principles of administrative decisionmaking. We contend that the court below failed to require the Commission to demonstrate the same caliber of reasoned decisionmaking on the rate of return issue as it required on the zone differential issue. This inconsistency in the reasoning of the court below is inexplicable, will lead to confusion in the future administration of the Natural Gas Act, and presents a question the resolution of which by this Court is imperative.

2. The Resolution Of The Questions Presented Is Necessary To Provide Guidance To Courts Of Appeals On The Proper Standard Of Review Of Administrative Decisionmaking

In its Petition, the Commission states that the importance of the case rests in the allegedly erroneous con-

struction of Sections 4 and 5(a) of the Natural Gas Act by the court below. (FERC Pet., pp. 7-9). However, it is Transco's view that, regardless of the correct interpretation of the statutory bases for Commission-initiated ratemaking imposed upon a natural gas pipeline, the instant proceeding presents the more fundamental question of the procedures which administrative agencies, specifically the Commission in this case, are required to observe when engaging in administrative ratemaking. This larger issue is extremely important because in complex and very technical rate proceedings before agencies, where a great deal of deference is typically afforded to the agency's expertise, effective judicial review is the *only* protection against arbitrary and potentially damaging administrative decisions. Strict adherence to the requirement of *reasoned* decisionmaking is, therefore, essential if judicial review is to be effective. Thus, the importance of the instant case not only rests in the proper construction of the provisions of the Act but also the adequacy *vel non* of the Commission's decisionmaking regardless of the outcome on review of the statutory issue.

This Court has consistently held that judicial review of the Commission's rate of return determinations under the "end result" principle set forth in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944), is not to be perfunctory. *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U.S. 581, 605 (1945). Rate of return determinations, no less than any other agency determination, must set forth the pertinent facts relied upon and the reasoning based on such facts which resulted in the agency's decision. *Permian Basin Area Rate Cases*, 390 U.S. 747, 792 (1968). Further, effective judicial review requires that the Commission's order itself evidence that the agency has engaged

in the fact-finding and reasoning requisite to sustaining the orders on review. It is self-evident that an appellate court cannot properly step in and supply the agency's missing rationale. *Securities and Exchange Commission* v. *Chenery Corp., et al.,* 318 U.S. 80, 88 (1943). The foregoing principles are applicable regardless whether the Commission was empowered to act under Section 4 of the Act, as the Commission and the other petitioners contend, or under Section 5(a), but the requirements are particularly important where, as in this case, the Commission proposes to set aside an established rate component.

That the Commission determined a so-called "zone" of reasonable rates of return — the limits of which were neither proposed by any witness nor explained by the Commission as being based on evidence in the administrative record — which was below the previously allowed 14.75 percent level of return is not an explanation of why the previous "just and reasonable" return allowed Transco has become "unjust, unreasonable, unduly discriminatory or preferential." As this Court held in *Mobile Gas*, 350 U.S. at 341, it is not the Commission's function to disregard the rates established by regulated pipelines but rather to review those established rates and, *only if they are found unjust or unreasonable,* is the Commission empowered to initiate new rates of its own design. At a minimum, therefore, effective judicial review of the rate of return order herein demands that the Commission have confronted head-on the issue of the reasonableness of Transco's established 14.75 percent return and, addressing this previous allowance on its merits, explained the basis, if any, for its conclusion that Transco's pre-existing 14.75 percent allowed equity return had become unlawful. Because the court failed to require such an explanation, evidencing the prefunctory

nature of its review of the Commission's decisionmaking, it is important that this Court establish firm guidelines for judicial review of Commission orders which purport to discard existing and lawful rates of return reflected in the rates of regulated companies and establish substantially lesser levels of return.

In Transco's view, effective judicial review of any Commission determination to reduce substantially a pipeline's previously allowed rate of return requires that the Commission make a threshold finding that changed circumstances require and support the proposed reduction. If established rate components are to be truly considered the point of departure in reviewing decisions to change such components, as the court below held in *Columbia Gas, supra,* the Commission, in cases where a reduction of previously allowed rates of return is contemplated, must offer or rely upon some proof that the pre-existing rate level allowed has become excessive and explain the reasoning which led to such conclusion. Stated differently, if effective judicial review depends on an explanation of why an existing and lawful rate level has become unlawful, then an explanation of the changes bearing on such a conclusion is indispensable to effective review.[9] The Commission's refusal to consider Transco's previously allowed 14.75 percent rate of return allowance in this case (App. C, p. 12a), therefore, should have been recognized by the court below as an insuperable barrier to effective judicial review of the Com-

[9] This requirement is consonant with that which the Commission requires of applicants for an increase in previous rate of return allowances where the burden of proof is on the applicant. *See, Minnesota Power & Light Co.* (Opinion No. 87), issued on June 24, 1980 in FERC Docket No. ER77-427, *mimeo*, p. 3; *see also, Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 236 F.2d 606, 612 (3d Cir. 1956).

mission's attempt to reduce Transco's previously allowed return on equity capital allowance and the court below should properly have reversed and remanded the Commission's rate of return orders. Since it did not, and because the court below arrogated to itself the task of supplying for the Commission the analysis requisite under settled law, this Court should, if it grants the Petitions filed on the zone differential issue, grant the instant Cross-Petition and clarify the correct standard of judicial review binding on courts of appeal concerning review of Commission decisionmaking under either Section 4 or Section 5(a) of the Act.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that in the event the Court should grant the Petitions for writs of certiorari in Nos. 80-1937, 80-1938 and 80-1939, this Cross-Petition for a writ of certiorari should likewise be granted.

Respectfully submitted,

BRIAN E. O'NEILL, *Senior Vice President and General Counsel*
R.V. LOFTIN, JR.
TRANSCONTINENTAL GAS PIPE LINE CORPORATION
P.O. Box 1396
Houston, Texas 77001

THOMAS F. RYAN, JR.
RICHARD T. BOONE
ANDREWS, KURTH, CAMPBELL & JONES
1747 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
(202) 861-7400

Attorneys for
Transcontinental Gas Pipe Line Corporation

June 17, 1981

APPENDIX

APPENDIX A

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. RP76-136 and RP77-26

Before Commissioners:

GEORGIANA SHELDON, *Acting Chairman;*
MATTHEW HOLDEN, JR.,
and GEORGE R. HALL.

TRANSCONTINENTAL GAS PIPE LINE CORPORATION (TRANSCO)

ORDER AFFIRMING AND ADOPTING INITIAL DECISION
(Issued August 30, 1979)

On February 13, 1978, the presiding administrative law judge issued an initial decision in the above-captioned proceeding as to the issues of rate of return on common equity and carrying charges on unrecovered demand charge credits. We agree with the initial decision on all questions presented and find nothing in the exceptions thereto warranting further discussion.

The Commission orders:

(A) The initial decision of the administrative law judge is affirmed and adopted.

(B) Within 60 days, Transco shall file revised tariff sheets and rates in accordance with the terms of the initial decision and of this order.

(C) Within 30 days after acceptance of the revised tariff sheets and rates submitted pursuant to paragraph (B) above, Transco shall refund to its jurisdictional customers all amounts collected in excess of the approved rates together with interest at the rate of nine percent per annum. Within

ten days thereafter, Transco shall submit a report setting forth the calculation of refunds and interest paid.

By the Commission.

(SEAL)

Kenneth F. Plumb,
Secretary.

APPENDIX B

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. RP76-136 and RP77-26

TRANSCONTINENTAL GAS PIPE
LINE CORPORATION (TRANSCO)

NOTICE OF DENIAL OF APPLICATION FOR REHEARING AND MOTION FOR STAY
(Issued October 24, 1979)

On September 28, 1979, Transco filed an application for rehearing and a motion for stay of the Commission's order, issued on August 30, 1979, in the above-referenced docket.

Take notice that the Commission agreed at its meeting of October 17, 1979, to take no action on the above-mentioned application for rehearing and motion for stay.

Accordingly, the application for rehearing is deemed denied under section 1.34(c) of the Commission's Rules of Practice and Procedure. (18 CFR §1.34(c)). The motion for stay is deemed denied under section 1.12(e) of the Commission's Rules of Practice and Procedure. (18 CFR §1.12(e)).

Kenneth F. Plumb,
Secretary.

APPENDIX C

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. RP76-136 and RP77-26

TRANSCONTINENTAL GAS PIPE LINE CORPORATION

INITIAL DECISION ON RESERVED ISSUES

(February 13, 1978)

APPEARANCES

Thomas F. Ryan, Jr., Robert G. Hardy and *Brian E. O'Niell* for Transcontinental Gas Pipe Line Corporation

John D. Daly, Jr., and *Giles D. H. Snyder* for Columbia Gas Transmission Corporation

Paul W. Fox and *John S. Schmid* for Delmarva Power & Light Company

Norman A. Flanigan, Charles R. Brown and *George L. Weber* for Consolidated Natural Gas Service Company, Inc.

Henry P. Sullivan for Consolidated Gas Supply Corporation

Edward S. Kirby, James R. Lacey, William R. Duff and *Carl W. Ulrich* for the Public Service Electric & Gas Company

Joseph P. Stevens, Barbara M. Gunther and *Michael W. Hall* for The Brooklyn Union Gas Company

John T. Miller, Jr., for Elizabethtown Gas Company

Stephen H. Watts II for Commonwealth Natural Gas Corporation

William I. Harkaway, Garrett Austin, G. Douglas Essy and *John M. Cutler, Jr.*, for Consolidated Edison Company of New York, Inc.

Richard A. Solomon, Sheila S. Hollis, Peter H. Schiff and *Dennis Lane* for the Public Service Commission of the State of New York

Dale A. Wright and *Gregory Grady* for Public Service Company of North Carolina, North Carolina Natural Gas Corporation, and Piedmont Natural Gas Company, Inc.

Susan A. Low for Washington Gas Light Company

John T. Stough, Jr., for Atlanta Gas Light Company

Ira G. Megdal for South Jersey Gas Company

Jack M. Irion for United Cities Gas Company

Linda S. Mounts and *Ronald D. Eastman* for Burlington Industries, Inc.

Richard A. Oliver, Richard P. Noland and *Edward J. Grenier, Jr.*, for Cannon Mills Co., Cone Mills Corporation, Nabisco, Inc., Pine Hall Brick & Pipe Corporation

Edward G. Bauer, Jr., Eugene J. Bradley and *Donald Blanken* for Philadelphia Electric Company

William J. Benham for Texaco, Inc.

Barry J. Hart and *Stephen Schachman* for Philadelphia Gas Works

Stephen Watts for CNG Transmission Company

Morton L. Simons for North Carolina Utilities Commission

Keith R. McCrea and *Wayne W. Whitney* for Corning Glass Works, Lithium Corporation of America, Sayles Biltmore Bleacheries, Inc., and The Torrington Company

Frederick H. Ritts for the City of Danville, Dan River, Inc., and Philip Morris, Inc.

Norman A. Pedersen and *Michael A. Kelly* for the Staff of the Federal Energy Regulatory Commission

GROSSMAN, PRESIDING ADMINISTRATIVE LAW JUDGE:

PROCEDURAL HISTORY

On July 30, 1976, Transcontinental Gas Pipe Line Corporation (Transco) tendered for filing in Docket No. RP76-136 revised tariff sheets reflecting an $81.3 million rate increase, based on the twelve months ending April 30, 1976, as adjusted for known and measurable changes through January 31, 1977. Transco requested that the proposed rate increase become effective on September 1, 1976. By order issued August 30, 1976, the Commission[1] accepted the revised tariff sheets for filing and suspended their use for five months until February 1, 1977, when they were permitted to become effective, subject to refund.

On December 30, 1976, Transco tendered for filing in Docket No. RP77-26 revised tariff sheets to increase its rates for interruptible transportation services rendered under Order No. 533[2] to various industrial consumers. Transco had been charging 22 cents per Mcf plus fuel and line loss for transporting "533" gas anywhere on its system and had not proposed to increase this rate in its filing in Docket No. RP76-136. Transco proposes to increase its rates for interruptible transportation to 28.2 cents per dekatherm (dth) in Transco's rate Zone 1, 28.8 cents per dth in Zone 2, and 31.5 cents per dth in Zone 3 plus fuel.

This increase in rates for transportation of "533" gas would result in approximately $275,000 in additional revenues annually, based on the test period volumes presented by Transco in Docket No. RP76-136. Transco requested an effective date of January 31, 1977. By order issued on January 31, 1977, the Commission accepted for filing the revised tariff sheets tendered December 31, 1976, and

---

[1] Commission refers to the Federal Power Commission prior to October 1, 1977, and to the Federal Energy Regulatory Commission thereafter.

[2] *Policy With Respect to Certification of Pipeline Transportation Agreements,* Docket No. RM75-25, Order No. 533, 6 F.P.S. 5-803 (August 28, 1975), *codified at* 18 CFR §2.79 (1977).

suspended them for one day, permitting them to become effective, subject to refund on February 1, 1977. Docket No. RP77-26 was consolidated with Docket No. RP76-136 for purposes of hearing and decision.

On March 30, 1977, Transco tendered for filing in Docket No. RP77-48 revised tariff sheets to increase further the rates for long haul interruptible transportation service to 42.8 cents per dth for Zone 1, 45.8 cents for Zone 2, and 49.4 cents for Zone 3 plus fuel. Transco requested an effective date of April 1, 1977. Transco also filed a request with the Administrator of the Emergency Natural Gas Act of 1977 (ENGA)[1] in Docket No. E77-83 to charge the Docket No. RP77-48 rates, effective April 1, 1977, for all ENGA gas which Transco purchases and transports as agent for certain of its customers and for all ENGA gas which Transco transports for others. Transco's prior practice had apparently been to transport emergency gas, whether purchased under Section 2.68 of the Commission's Regulations or ENGA, without charge other than for fuel and line loss.

The Administrator initially allowed Transco to charge the rates filed in Docket No. RP77-48. *Emergency Order Pursuant to Section 6 of Pub. L. 95-2,* Docket No. E77-83, April 4, 1977. By letter dated April 27, 1977, however, the proposed rates in Docket No. RP77-48 were rejected by the Commission for noncompliance with Section 154.63 of the Commission's Regulations. On May 23, 1977, the Commission denied Transco's application for rehearing of the rejection. Accordingly, on June 1, 1977, in Docket No. E77-83 Transco proposed new, lower transportation rates for ENGA gas, effective April 1, 1977, equivalent to the rates in effect subject to refund in Docket No. RP77-26. On June 10, 1977, the Administrator approved these lower rates, stating that such rates would be collected subject to refund pending resolution of the transportation rate issue in Docket Nos. RP76-136 and RP77-26. *Supplemental Emergency Order*

---

[1] Act of February 2, 1977, Pub. L. No. 95-2, 91 Stat 4.

Pursuant to Section 6 of Pub. L. 95.2, Docket No. E77-83, June 10, 1977.

On June 28, 1977, Piedmont Natural Gas Company, Inc., Public Service Company of North Carolina, Inc., and North Carolina Natural Gas Corporation (North Carolina Companies) filed a motion requesting that the Commission order Transco to reduce its interruptible transportation rates to levels which would not result in the recovery of revenues in excess of Transco's claimed cost of service in Docket No. RP76-136, and to refund all excess revenues. By order issued October 31, 1977, the Commission denied the North Carolina Companies' motion noting that if the motion were granted, the rate for certificated interruptible transportation service would be 22 cents per dth and the rate for transportation of ENGA Gas would effectively be zero. The Commission in *Crab Run Gas Company, et al.,* Docket No. CP76-24, *et al.,* Order issued July 22, 1976, had found the 22 cents per dth rate is less than fully compensatory. The Commission concluded,

> Under the complex and unusual circumstances presented in this case, the Commission's authority to order refunds, with interest, of all amounts in excess of Transco's claimed cost of service in Docket No. RP76-136, and its power to order the additional refund, with interest, of all amounts ultimately found not to be justified, is sufficient to protect the public interest.

Transcontinental Gas Pipe Line Corporation, Docket Nos. RP76-136 and RP77-26, Order issued October 31, 1977, mimeo ed. at 6.

A prehearing conference was convened on January 4, 1977. On July 25, 1977, following settlement conferences and the filing of prepared direct testimony, a hearing was convened for the purpose of submission of evidence and cross-examination. The hearing in this case was phased so that at the session commenced on July 25, 1977, cross-examination was conducted only on cost of service issues. Rate design

issues, including the issue of interruptible transportation rates, were deferred until September 27, 1977. The July 25, 1977, cost of service phase of the hearing lasted two days and resulted in 609 pages of transcript: Volume 2, pages 9-459 and Volume 3, pages 460-618.

The rate design phase of the hearing was convened on September 27, 1977, but was recessed for the purpose of allowing further attempts to achieve a settlement. On November 1, 1977, the parties appeared before the Presiding Judge to request certification of a proposed settlement agreement (Exhibit 51) to the Commission for its consideration and disposition.

The proposed agreement resolved all issues which had arisen in this proceeding except four: (1) rate base treatment of certain advance payments, (2) rate base treatment for unsuccessful alternate gas supply costs, (3) rate of return on equity and (4) carrying charges on unrecovered demand charge credits. The issue of rate base treatment for certain advance payments was severed from this proceeding by order issued October 21, 1977, and is to be resolved in the consolidated proceeding in *Transcontinental Gas Pipe Line Corporation,* Docket Nos. RP74-48 and RP75-3 (AP76-1), *et al.* The unsuccessful alternate gas supply costs issue is to be determined by the outcome of *Transcontinental Gas Pipe Line Corporation* v. *Federal Energy Regulatory Commission,* No. 77-1712 in the United States Court of Appeals for the District of Columbia Circuit. The remaining two issues of rate of return and carrying charges on unrecovered curtailment credits are reserved and are the subjects of this decision.

On November 3, 1977, the Presiding Administrative Law Judge certified the proposed settlement agreement and the associated record to the Commission. Initial comments on the agreement were filed on November 16, 1977. Transco, Staff, and all but three parties either supported the settlement agreement in its entirety or did not oppose the agreement. Additionally, Mesa Petroleum Company filed a petition to intervene out of time and a comment opposing Article V of

the agreement regarding a "tracking" of advance payments.

In the November 3, 1977, certification of the proposed settlement agreement, the Presiding Judge as required by the Rules of Practice, also reported to the Commission an oral motion made by Counsel for the North Carolina Utilities Commission pursuant to Section 1.30(c) of the Commission's Rules of Practice and Procedure for omission of the initial decision on the two reserved issues of rate of return and carrying charges on unrecovered demand charge credits. The Commission has not issued an order on the proposed settlement agreement, although the motion for omission of the initial decision was denied. Order Denying Motion to Omit Initial Decision, issued December 19, 1977.

On July 1, 1977, Transco tendered for filing in Docket No. RP77-108, a proposed $50.8 million rate increase. Transco requested that the rate increase become effective on August 1, 1977. By order issued on July 20, 1977, the Commission accepted the proposed rate increase for filing and suspended it for five months until January 1, 1978, when it will be permitted to become effective, subject to refund. Accordingly, as of January 1, 1978, the rates proposed in Docket No. RP76-136 and RP77-26 will be for the "locked-in" period February 1, 1977 to December 31, 1977.

Initial briefs on the reserved issues were filed by Transco, Staff, The Public Service Commission of the State of New York (NYPSC), and the North Carolina Utilities Commission (NCUC). Briefing was completed by the filing of reply briefs by the same parties on January 27, 1978.

TRANSCO'S RETURN ON EQUITY

Transco seeks a return on equity of 17.0%. Based on the January 31, 1977, capital structure presented by Staff witness

Adelman,[4] an overall return of 10.12% would result. Staff argues the return on equity should be 14.0%, yielding an overall return of 9.39%. The NYPSC urges adoption of a rate of return on equity between 13.5 and 13.75%, while the NCUC contents itself by demanding a rate "not to exceed the just and reasonable level." No specific rate is proposed, but clearly the NCUC believes it to be somewhat less than 13.5%.

We start from the premise that a pipeline will recover all its allowed cost of service, including a just and reasonable return, if its cost-based rates are set by allocating properly the pipeline's costs to the volumes to be sold or transported within the period at issue. Whether the pipeline operates at 100% capacity or, as Transco, operates at 50% capacity under seasonal curtailment, full recovery of costs and return will result if the projected costs and volumes are accurate.[5]

Transco states it has no reason to suspect the accuracy of its projections as to costs and volumes. It is assumed the tendered settlement agreement, which includes agreement as to cost of service issues, reasonably reflects Transco's projections. The risk to Transco's investors is that the projected volumes are too high or the projected costs too low. The risk to Transco's ratepayers is precisely the opposite.

---

[4]

	Amount	Ratio	Cost	Weighted Cost
	(000)			
Long-Term Debt	$ 952,614	63.02%	7.92%	4.99%
Preferred Stock	192,146	12.71	8.12	1.03
Account 281	2,630	0.17	-0-	-0-
Common Equity	364,154	24.10		
Total	$1,511,544	100.00%		

Exhibit 17, p. 1.

[5] NCUC argues Transco's operation at 50% capacity indicates lack of efficient and economical management and should not be rewarded. The record is barren of evidence to support such a charge and it will not be considered further.

These risks, among others, must be balanced in determining the rate of return on equity to be allowed Transco.

Transco premises its request for a 17% return on the arguments that gas supply to the Transco system is critical and is a risk falling mainly on investors; that Transco's capitalization (24.10% common) is the thinnest of any major pipeline, thus deserving of a high return and that Transco should be equated to the "higher earner" electric utilities for purposes of determining a just and reasonable return.

Transco's witness Field refers to recommended (or at least accepted) rates of return on common equity of 14.75% in each of Transco's last three rate cases, all of which were settled. In the first two (RP74-48 and RP75-3), common equity ratios were 23.69%; in the third (RP75-75), the ratio was 25.10%. (Transco questions any Staff position arguing for a return of less than that agreed to in the three settled cases.) Having stated Transco's contention, it will not be considered. Settlements are precisely that which they are intended to be—disposition by agreement, doing no violence to the public interest. They are not in any respect precedential, nor should they be. There exists no basis to determine how they were reached, what compromises, if any, were made, or on what reasoning they were accepted. Transco's requested return will have to be justified, if it can be, on other grounds.

Transco's concern for future earnings is summarized by witness Field:

> My major worry is five years down the road, 10 - 15 years down the road, will we in our cost calculations derive costs and derive prices to recoup those costs which will, when the market test is applied, allow the company full cost of service recoupment.

Certainly, this would be a valid, and perhaps overriding concern were rates here proposed for a period of ten or more years. This, however, is not the case. It is obvious that we are dealing here with a locked-in period of only 11 months, and

there is nothing to suggest Transco intended the effective period of the rates in question to be longer, much less the 10 - 15 year period forecast. Inasmuch as annual (or more frequent, if possible) filings are the norm, projections are constantly revised, refined and updated. The risk inherent in inaccuracy is soon subject to correction. Thus, we deal not with possibilities of the distant future but with probabilities of annual projections. As long as this situation persists, the basic premise warrants that accurate projections will yield full return.

Although Transco faces formidable gas supply problems, it faces no risk that whatever volumes it has will not be sold. To the extent competition is a factor with respect to Transco's system, it is the competition among Transco's customers for Transco's gas.

Transco attempts to equate the risks it faces to those faced by electric utilities. In so doing, witness Field draws an analogy between Transco and the "higher earners" among the electrics. Unless the Commission is to abandon the historic distinction in return determinations between gas and electric utilities, and unless one were to ignore completely the extreme capital intensive nature of an industry required by law to meet projected demand, Transco's argument simply cannot be accepted. The Presiding Judge is not prepared even to recommend that the Commission consider such a departure from historic practices of rate making.

Finally, Transco, on brief, refers to recent Commission opinions authorizing returns as high as 13.50% and 13.75% on common ratios higher than that of Transco. This, perhaps, might support a requested return in that range; it certainly lends no support to Transco's requested 17% return.

Transco's requested return on common equity is without reasonable justification by Transco, and certainly no other party supports that rate. There is no other conclusion to be reached other than that there is no evidence present to support the requested rate of return.

Staff urges 14% as a just and reasonable return. Citing the ever present tests enunciated by the Supreme Court in the *Hope* and *Bluefield* cases,[6] witness Adelman equated the business and financial risks of Transco to those of comparable utility groups, selecting, for comparison, the familiar Moody's 24 Utilities, FPC Class A & B Electrics, and FPC Major Class A & B Pipelines. His analysis, and in particular his conclusion that Transco, except for the exceptionally poor year of 1974, has kept pace with or exceeded the Major A & B Pipelines and the two electric groups in terms of return average on common equity. Witness Adelman concluded that Transco's decision to seek additional gas supply, rather than invest that capital in diversification into non-regulated ventures, makes it a somewhat greater risk than would be an average pipeline. Based upon his analysis, and consideration of allowed returns to other pipelines and their common equity ratios, a rate of return on common equity of 14% is recommended by Staff.

NYPSC urges a return of between 13.5 and 13.75%, discounting the consideration of Transco's thin equity ratio in Staff's presentation. It argues that Transco's achieved earnings per share, which have risen from $2.01 in 1975 to $2.21 in 1976 and to $2.40 for the first half of 1977, coupled with large investment tax credits, offset the risk commonly considered inherent in a thinly capitalized enterprise. Thus, it is argued, lower risk warrants lower return.

NCUC, as noted, opposes all proposed rates of return, but does not suggest what it considers proper. Nor does it set forth any criteria designed to enable a rational determination.

Upon consideration of the record and the positions of the parties summarized above, it is concluded that Transco poses greater risks to investors than does virtually any other pipeline company, but that these risks are not of such magnitude as to

---

[6] *F.P.C.* v. *Hope Natural Gas Company*, 320 U.S. 591 (1944). *Bluefield Water Works and Improvement Company* v. *Public Service Commission*, 262 U.S. 679 (1923).

warrant significant departure from comparable ventures having somewhat fewer risks. Transco's ability not only to survive but to achieve modest prosperity in the face of its severe gas supply situation attests to its inherent strength in the marketplace. For a company such as Transco, a relatively narrow zone of reasonableness exists within which a just and reasonable rate of return on equity should be. That zone extends from 13.50%, below which the return to Transco would be below that available on investments in other enterprises having corresponding risks, and confidence in its fiscal integrity would not be assured, and 14.30%, above which the return to Transco would be excessive at the expense of the ratepayers.

Within this zone, the capital structure and risk analysis of Transco justify determination of the rate of return to be allowed on common equity at 14%, slightly higher than the midpoint of the zone of reasonableness, and amply supported by Staff's analysis.

INTEREST ON UNRECOVERED DEMAND CHARGE CREDIT BALANCE

Transco extends a credit on each customer's demand charges to the extent that the customer is curtailed. This credit is recovered by Transco through a surcharge on volumes of gas actually delivered, thus distributing the burden of curtailment more evenly.

As originally proposed, Transco includes the balance of unrecovered demand charge credits in working capital. Staff opposes rate base treatment for the unrecovered demand charge credits. NYPSC and NCUC do not take any position on this matter. Staff witness Chinn noted that the Commission's Regulations do not provide for carrying charges in the form of return and taxes on the balance, and observed that Transco can eliminate the problem of carrying an unrecovered curtailment credit balance by amending its tariff to allow "current collection" of credits. The tariff provision would allow Transco to estimate the credits it will be

extending in a month and estimate the actual sales during the month to enable Transco's recovery of the amount credited during the month in which the credit is extended.

Transco's witness Mullendore indicated Transco would accept a tariff revision to provide for "current collection" as an alternative to its originally proposed inclusion of the unrecovered demand charge credit balance in working capital.[7] Switching to the "current collection" basis, however, would, as of the day of the switch, leave Transco holding an unrecovered balance in its deferred account for demand charge credits. Transco proposes to recover this "locked-in" balance by way of a surcharge which would appear on customers' bills for each of the six months following effectiveness of the tariff. Transco proposes to collect interest on the balance until it is amortized through the surcharge.

Transco asserts that allowance of carrying charges is the necessary and proper rate treatment to make Transco whole with respect to its costs associated with unrecovered demand charge credits. To the extent that recovery of demand charge credits has been deferred, Transco claims it has collected less revenues than necessary to recover its current costs, thus resulting in costs for which Transco should be compensated.

Staff does not oppose Transco's surcharge proposal, but does oppose the proposal to collect interest on that balance. Staff notes the amount on which Transco seeks to collect

---

[7] The Settlement Agreement in these dockets, pending Commission action, provides for Transco to file revised tariff sheets reflecting rate recovery of curtailment credits on a current basis. Such filing was made December 1, 1977, in Docket No. RP78-25, wherein Transco filed revised tariff sheets proposed to be effective January 1, 1978, to provide current recovery and for collection of carrying charges at 9% per annum on the unrecovered curtailment credits during the period February 1, 1977, until the unrecovered balance is eliminated at July 1, 1978. In its filing, Transco agreed that collection of such carrying charges, which total $1,469,672, would be subject to refund with interest, depending on the outcome of the reserved issue herein.

interest is not an amount which was borrowed nor on which Transco is paying any carrying charges. (Transco's customers were never billed this amount, nor was it owed by them.)

Staff argues Transco should not be allowed interest on the "purely paper" amount of accumulated unrecovered demand charge credits. Staff claims Commission policy is clear: carrying charges are not to be allowed on deferred account balances. For example, it notes, "carrying charges will not be allowed on any balances pertaining to unrecovered purchased gas costs" 18 C.F.R. 154.38(d)(4)(iv)(c) (1977). Staff analogizes the instant proposal to the "fuel surcharge" situation in Opinion No. 790, *Public Service Company of New Hampshire,* Docket No. ER76-285 (March 21, 1977); *Maine Public Service Company,* Docket No. E-8264 (June 27, 1977); and *Virginia Electric Power Company,* Docket No. ER76-415 (June 20, 1977). It asserts the unrecovered curtailment credit balance here is, in material respects, similar to the locked-in deferred fuel cost balances at issue in those cases. (If the entire surcharge to recover the unrecovered fuel cost balance were disallowed in those cases, Staff contends, interest should not be allowed here.) Transco agrees that Section 154.38(d)(4)(iv)(c) of the Commission's Regulations does not permit carrying charges on any balances of unrecovered purchased gas costs. It argues, however, that this establishes no policy in this area because in Order No. 452-A, the order on rehearing of the order adopting the PGA regulations, the Commission stated (37 F.R. 12489, June 24, 1972):

> El Paso Natural Gas Co., and Columbia Gas Transmission Corp., object to carrying charges not being allowed on balances pertaining to unrecovered purchased gas costs. El Paso suggests that these amounts constitute working capital. Ratemaking treatment of this item shall be considered on the merits when the issue is raised in rate proceedings for individual companies. The last sentence of §154.38(d)(4)(iv) will be changed by omitting reference to excluding amounts in Account 186 from rate

base. It should be noted that this subsection does not require interest to be paid by companies with excess balances.

Staff's reliance on three "fuel surcharge" cases involving attempts by electric utilities to collect a fuel surcharge is misplaced, according to Transco, because those cases did not involve interest or carrying charges, but rather the justification for collecting a fuel surcharge. In summary, Transco argues Staff has not justified denial of the carrying charges on unrecovered demand charge credits.

Whether Staff has or has not justified denial of the sought imposition of carrying charges is not the threshold question. That question properly is whether Transco has justified inclusion of the carrying charges.

In the absence of any clear policy or regulation, and treating the matter individually on the merits presented here, in accordance with the general guidance of Order No. 452-A, it is clear that Transco, having the burden of proving the provision to be just and reasonable, has failed to do so. (Merely to aver a provision is appropriate because nothing specifically prohibits it is no showing at all.) Contrary to Transco's claim, denial of inclusion of interest on carrying charges will not result in any cost for which Transco will not be compensated. Denial of interest on carrying charges means only that Transco will be compensated fully for the carrying charges but will not be allowed an additional return on them in the form of interest. If interest on carrying charges is analogous to any other sought recovery, it is analogous to the "fuel surcharge" situation, despite Transco's protestations. Just as in the case of fuel adjustments, carrying charges could have been billed and collected on a current basis. That Transco chose not to do so until now does not create justification to expose ratepayers to additional liability.

Transco, therefore, shall eliminate from its filing any interest charges on unrecovered demand charge credit balances.

ULTIMATE FINDINGS AND CONCLUSIONS

(1) Applicant, Transcontinental Gas Pipe Line Corporation, is a "natural gas company" subject to the provisions of the Natural Gas Act, and the sales of natural gas subject to the order which follows as a part of this Decision are sales of natural gas in interstate commerce for resale subject to the jurisdiction of the Commission.

(2) The increased rates, which are the subject of this Decision, except to the extent heretofore specifically disapproved, are shown to be just and reasonable, and to the extent heretofore specifically disapproved, are found to be excessive.

(3) The just and reasonable rates and charges are, under the applicable provisions of the Natural Gas Act, those which are in conformity with the views, findings and conclusions set forth in the Decision herein.

WHEREFORE, IT IS ORDERED, subject to review of the Rules of Practice and Procedure of the Commission, that:

(A) Within 30 days from the issuance of this Decision or final disposition of the above-described Settlement Proposal, whichever is later, Transcontinental Gas Pipe Line Corporation shall refund to its customers any amounts collected in excess of those found just and reasonable as specified in the discussion above, together with interest from the date of payment to the date of refund, at the interest rate prescribed by the Commission's Regulations as amended on July 14, 1976, in Docket No. RM74-18, Order No. 513-A.

(B) Within 30 days after making the refunds required by paragraph (A), Transcontinental Gas Pipe Line Corporation shall file with the Commission in writing and under oath, a report as to the amount of refunds made and the method of their calculation, together with releases from all customers to whom refunds have been made.

/s/ STEPHEN L. GROSSMAN
Stephen L. Grossman
Presiding Administrative Law Judge